manufacture competitive "harms." As detailed below, there is no merit to these claims, each of which takes great liberties with the relevant facts, fundamental economic principles or both. In each case, the goal is the same: to sabotage the increased competition that the merger promises. As ILEC and AOL executives recently, and perhaps a bit too candidly, remarked of their unholy alliance: our "big idea? Get the feds to hobble AT&T in the name of 'consumer choice.'"[60]

A. The Merger Will Have No Material Impact In The Video Programming Market.

1. The Merger Will Not Materially Impact Video Programming Concentration.

Competition in the video programming business is exploding.[61] There are currently over 245 national satellite-delivered video services, up from 172 in 1997.[62] Many of these are owned by large, well-funded and experienced media companies. And of the 245 national services, 61 percent are not owned by *any* MSO.[63] Furthermore, the Commission has identified 65 planned national programming services that are expected to launch in the near future.[64] The proposed Merger will have no anticompetitive effects in this highly dynamic market.

Recognizing this, Opponents concoct an entirely different (and imaginary) merger to challenge. More specifically, Consumers Union ("CU") and Bell Atlantic contend that this Merger somehow combines all the programming interests held by AT&T, MediaOne, Liberty

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[60] P. Kiger, *George Vradenburg's Potomac Fever*, Regardie's Power, at 85 (Sep./Oct. 1999).

[61] Public Interest Statement at 44-45.

[62] Fifth Annual Report, *Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, FCC 98-335, ¶ 159 (rel. Dec. 23 1998) ("*Fifth Annual Video Competition Report*").

[63] *Id.*

[64] *Id.* ¶ 168.

Media Group ("Liberty"), TWE, and Cablevision.[65] As demonstrated below and in the attached report by Charles River Associates, that claim is indefensible.[66]

AT&T neither controls nor has an economic interest in Liberty. Liberty's programming interests thus do not and cannot increase AT&T's power – whether pre- or post-Merger – in the video programming business. Moreover, AT&T's post-Merger ownership interests in the video programming held by TWE and Cablevision will be only passive economic interests that give AT&T no programming involvement.[67] Any economically meaningful measurement of market concentration must reflect differences between control and mere economic interest: although the investor may alter its *own* behavior as a result of the acquisition of a mere economic interest in another firm, the investor cannot directly affect the behavior of the firm itself.[68] These facts make clear that the Merger will have no material impact on video programming concentration. Opponents simply ignore them.

a. AT&T's ownership of Liberty does not affect AT&T's incentive or ability to act in an anticompetitive manner.

Unable to point to any basis in logic or economic theory, Opponents resort to mischaracterizing statements of the Commission and Department of Justice ("DOJ") to support

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[65] Bell Atlantic at 2-6; Consumers Union, *et al*, *Breaking the Rules: AT&T's Attempt to Buy a National Monopoly in Cable TV and Broadband Internet Services*, at 52-55 ("Cooper Report").

[66] S. Besen, S. Moresi & J. Woodbury, *An Economic Analysis of the Effects of the AT&T-MediaOne Merger on Competition in the Supply and Distribution of Video Programming Services: Response to the Critics* ("CRA Report").

[67] MediaOne's remaining programming interests are very limited. *See* Public Interest Statement at 17.

[68] *See* CRA Report at 7-8.

their assertion that AT&T controls and has an economic interest in Liberty.[69] But, as Professor Coffee explains in his supplemental declaration, the fact that the Commission and DOJ have stated that Liberty is in some sense a "subsidiary" of AT&T, and that AT&T has an attributable interest in Liberty for purposes of the program access rules, does *not* mean that AT&T has an "economic" interest in Liberty that would create an incentive for AT&T to act anticompetitively toward unaffiliated programmers or competing MVPDs. AT&T's ownership of Liberty has been structured to ensure that: (1) Liberty and AT&T are, and will remain, economically distinct entities; and (2) Liberty is and remains operationally independent from AT&T. Thus, any anticompetitive action that AT&T might take to benefit Liberty (*e.g.*, foreclosing video programmers that compete with Liberty) cannot possibly benefit AT&T, because AT&T has *no* right to participate in any increased revenues or value Liberty might realize from such foreclosure.[70] Similarly, Liberty has no incentive to take any action to benefit AT&T (*e.g.*, by refusing to sell programming to an MVPD that competes with AT&T), because Liberty does not participate in AT&T's increased revenues or value. Finally, because AT&T and Liberty are operationally independent, neither can compel the other to take such actions, even if they had incentives to do so.

[69] *See* Bell Atlantic at 4-5; U S West at 12.

[70] *See* Supplemental Declaration of John C. Coffee, Jr. ¶ 16 ("Coffee Supp. Decl.") ("I do not believe there is any realistic way that AT&T can dominate or control the Liberty board of directors, divest assets or earnings from Liberty to itself, or receive any material economic benefit from its ownership of Liberty. In turn, this implies that, having no economic incentive to control Liberty, AT&T should be rationally indifferent as to the management policies and practices that Liberty follows.").

In short, AT&T's ownership of Liberty is irrelevant to an analysis of AT&T's impact on the video programming market because that ownership does not affect AT&T's incentive or ability to act in an anticompetitive manner.

AT&T and Liberty are economically distinct. The Commission's statement that Liberty is a subsidiary of AT&T is not inconsistent with the fact that AT&T has no economic interest in Liberty. Liberty is a subsidiary of AT&T because AT&T indirectly owns 100 percent of the outstanding capital stock of Liberty Media Corporation ("LMC"), which, in turn, owns substantially all of the assets of Liberty. However, this does not give AT&T an economic interest in Liberty because AT&T's ownership of Liberty has been specifically structured to ensure that the economic interests of AT&T and Liberty are totally separate.[71]

Most importantly, all dividends and distributions by Liberty must be passed through to its tracking stock shareholders, not to AT&T.[72] Thus, AT&T has no ability to participate in any distribution of profits earned by Liberty and will receive no benefit from increasing Liberty's revenues. Moreover, because the value of Liberty's assets are represented by the value of the Liberty tracking shares, any appreciation in the value of Liberty and/or its assets will be reaped by the Liberty tracking stock shareholders, not by AT&T.[73]

[71] *See* Coffee Supp. Decl. ¶ 16.

[72] The Liberty tracking stocks are *not* held by AT&T (or any of AT&T's affiliates). Rather, the stocks are held by the former TCI-Liberty tracking stock shareholders and others that have purchased the publicly-traded Liberty shares since the merger of AT&T and TCI. *See* Coffee Supp. Decl. ¶ 3.

[73] *See id.* ¶¶ 10, 12-13.

Other constraints on AT&T's ownership of Liberty prevent any indirect participation in Liberty's assets or earnings. For example, AT&T may not "unwind" its ownership of Liberty except by a spin-off to the Liberty tracking stock shareholders, and AT&T cannot authorize new Liberty tracking stock, or dispose of Liberty's underlying assets, without the consent of the Liberty shareholders.[74] This same analysis applies in reverse, *i.e.*, Liberty owns no interest in AT&T and therefore has no incentive to take anticompetitive actions to benefit AT&T.[75]

AT&T cannot compel Liberty to undertake actions to favor AT&T. AT&T and Liberty also lack the means to cause one another to take anticompetitive actions to benefit the other. Indeed, AT&T's relationship with Liberty has been structured to provide Liberty with operational independence from AT&T. The Liberty officers and Board of Directors decide Liberty's course autonomously – without considering the interests of AT&T. For seven years following the Merger, a majority of LMC's board will be individuals who were on the LMC board prior to the Merger (or will be selected by pre-Merger incumbents).[76] Liberty and AT&T can compete with each other in their lines of business and have no obligation to provide financial support, share corporate opportunities, or otherwise assist each other. Likewise, Liberty has complete control over its own financing capability and other corporate matters. In short, Liberty and AT&T are operationally independent entities such that neither company can control the decisions of the other.[77]

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[74] *See id.* ¶¶ 8-9.

[75] *See id.* ¶ 13.

[76] *See* Coffee Supp. Decl. ¶ 12.

[77] *See* Coffee Supp. Decl. ¶ 13.

The DOJ has not found that AT&T controls Liberty. Bell Atlantic is dead wrong when it asserts that "[t]he Department of Justice has . . . found that AT&T controls Liberty."[78] The DOJ in its Competitive Impact Statement regarding the AT&T-TCI merger observed that "Liberty will be a wholly-owned subsidiary of AT&T Corp." This statement, while true, does not mean that AT&T *controls* Liberty. As shown above, ownership is not the same as control, and AT&T has no ability to control Liberty. The DOJ recognized as much. In its Competitive Impact Statement, DOJ noted that the relationship between AT&T and Liberty promoted a "hold separate" relationship justifying an extended divestiture period for Liberty's Sprint PCS interest.[79] Thus, far from concluding that AT&T controls Liberty, the DOJ has properly recognized that the operations of Liberty and AT&T are separate (and the consent judgment requires that this separation remain in place).[80]

b. This is not a merger of TWE and Cablevision.

CU's claim that the Merger is a complete merger of AT&T, MediaOne, TWE, and Cablevision is likewise unfounded.[81] AT&T's post-Merger interests in the programming services of TWE and Cablevision are only partial economic interests and AT&T will have no involvement in programming decisions.[82]

[78] Bell Atlantic at 5.

[79] *See* Competitive Impact Statement at 12-13, *U.S. v. AT&T Corp.*, No. 1:98CV03170 (D.D.C. filed December 30, 1998).

[80] *See* Coffee Supp. Decl. ¶ 14.

[81] *See* Cooper Report at 54.

[82] To the extent CU suggests that Comcast's programming interests are relevant here, Cooper Report at 54, this claim should be rejected out of hand. AT&T's agreement with Comcast pertains only to cable system swaps. Moreover, the ultimate arrangements by which certain cable systems will be swapped between Comcast and AT&T following the closing of the Merger (continued . . .)

There is ample reason for treating AT&T's post-Merger minority limited partnership interest in TWE as a silent interest for measuring concentration in the video programming marketplace.[83] This is so because Time Warner manages the day-to-day operations of TWE, and Time Warner's representatives to the TWE Board can take action unilaterally, without consent or participation by MediaOne, or even notice to MediaOne.[84] "AT&T and MediaOne simply do not have the power to control decisions, policies, or practices of TWE, and, indeed, have no involvement in day-to-day management of TWE cable operations."[85]

Additionally, MediaOne's August 3, 1999 termination of a noncompete clause between MediaOne and TWE, triggered a provision of the TWE partnership agreement that further limits MediaOne's – and therefore AT&T's post-Merger – rights. As described in Time Warner's recent filing to the SEC:

> As a result of the [non-compete] Termination Notice and the operation of the Partnership Agreement governing TWE, *MediaOne's governance and management rights have*

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have not been determined, and no application for such transfer is before the Commission in this proceeding or elsewhere.

[83] Equally important, the acquisition does not increase AT&T's interest in the Time Warner program services that are held outside TWE, most importantly the Turner services (for example, CNN, TNT, and the Cartoon Network). CU, however, attributes these interests as well to AT&T.

[84] *See generally* Declaration of John C. Coffee, Jr. ("Coffee Decl."). MediaOne has never participated in a Board meeting, and, to the best of MediaOne's knowledge, the TWE Board has never met. Post-Merger, AT&T will have the right to appoint two of six members to the TWE Board. However, the two AT&T board members will amount to nothing more than the means by which AT&T will be allowed to exercise certain rights designed to protect its minority investment in TWE. In fact, as described below, these protective rights are consistent with those the Commission generally permits for insulated limited partners and in no way implicate involvement with TWE's programming or other assets.

[85] Coffee Decl. ¶ 27.

terminated immediately and irrevocably to the fullest extent permitted by Section 5.5(f) of the TWE Partnership Agreement. As a result, *MediaOne no longer has a vote on or any right to participate in the Cable Management Committee* described on page I-21 of TWE's Annual Report on Form 10-K for the year ended December 31, 1998, *and its representatives serving on TWE's Board of Representatives no longer have the right to vote on any matter pertaining to any of TWE's businesses.* MediaOne retains certain protective governance rights on the TWE Board of Representatives pertaining to certain limited matters affecting TWE as a whole.[86]

In other words, Time Warner will bring matters to the attention of AT&T's representatives on the TWE board only when such matters fall within the scope of AT&T's very limited investor rights, which, as Professor Coffee explains, are characteristic of a limited partner with no control.[87]

In fact, because AT&T post-Merger will not be involved, directly or indirectly, in the management or operation of the media-related activities of TWE, AT&T believes that its interest satisfies the Commission's requirements for an insulated limited partnership. The Commission has enumerated seven factors[88] that will ensure that a limited partnership interest is insulated.[89]

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[86] Time Warner Entertainment Company, L.P., Securities and Exchange Commission Form 8-K (filed Aug. 5, 1999), at 3 (emphasis added).

[87] *See* Coffee Decl. ¶ 27.

[88] *See* 47 C.F.R. § 76.501, note (g)(2) (*citing* Memorandum Op. and Order, *Reexamination of the Commission's Rules and Policies Regarding the Attribution of Ownership Interests in Broadcast, Cable Television and Newspaper Entities*, 58 Rad. Reg. 604 (1985), *as modified on reconsideration*, Memorandum Op. and Order, 1 FCC Rcd. 802 (1986)). Specifically, the partnership documents should: (1) specify that the exempt limited partner cannot act as an employee if his functions relate to the partnership's media enterprises; (2) bar the exempt limited partner from serving, in a material capacity, as an independent contractor or agent regarding the partnership's media enterprises; (3) restrict the exempt limited partner from communicating with others regarding the day-to-day operations of the partnership's business; (4) empower the general partner to veto the admission of additional partners admitted by the exempt limited partner; (5) prohibit the exempt limited partner from voting on the removal of the general partner, or limit this right to situations where the general partner is subject to bankruptcy proceedings, adjudged incompetent by a court, or is determined incompetent by an independent third party; (6) bar the exempt limited partner from performing services to the partnership that relate to the partnership's

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The facts provided above demonstrate that the post-Merger rights and activities of AT&T with regard to TWE conform to these seven factors, and thus AT&T's post-Merger interest in TWE will be adequately insulated for purposes of the Commission's attribution rules.[90]

Specifically, the approval rights that MediaOne has – and AT&T will have after the Merger – are limited to fourteen items, all of which are consistent with an insulated limited partnership interest.[91] The Commission has found that the inclusion of all of these approval rights in either corporate or LLC documents does not lead to a finding of attribution.[92] In particular, the Commission has ruled that "[t]he right to participate in matters involving extraordinary corporate actions . . . does not ordinarily undermine the nonattributable character of otherwise noncognizable interests, so long as the voting rights or licensee obligations are

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media activities, with the exception of loaning money or acting as a surety for the partnership; and (7) state, in express terms, that the exempt limited partner is prohibited from becoming actively involved in the management or operations of the partnership's media businesses. *Id.*

[89] While limited partners generally will be adequately insulated if the partnership documents address the seven insulation criteria, a limited partner can demonstrate insulation when the attribution criteria are not specifically delineated in the limited partnership agreement. *See, e.g.*, Memorandum Op. and Order, *Application of Sacramento RSA Limited Partnership*, 9 FCC Rcd. 3182, ¶ 12 n.18 (1994).

[90] It is important to note that the foregoing analysis regarding the *de minimis* impact of AT&T's interest in TWE vis-a-vis a video concentration analysis does not depend on the Commission concluding that AT&T's interest in TWE qualifies as an insulated limited partnership interest.

[91] *See* Coffee Decl. ¶ 18.

[92] *See* Memorandum Op. and Order, *Applications of Roy H. Speer, Transferor, and Silver Management Company, Transferee*, 11 FCC Rcd. 14147, ¶ 18 (1996); *see also* Memorandum Op. and Order, *Applications of Quincy D. Jones, Transferor, and Qwest Broadcasting, LLC, Transferee*, 11 FCC Rcd. 2481, ¶ 9 (1995) ("*Jones-Qwest Order*").

narrowly circumscribed."[93] AT&T's approval rights post-Merger are the very type of narrowly circumscribed shareholder rights that are permitted under the Commission's attribution criteria.

Finally, AT&T's interest after the Merger in certain cable programming entities that sell programming to TWE should not disrupt the insulation of AT&T's interest in TWE; as demonstrated above, Liberty operates independently from AT&T. Liberty's sale of programming to TWE should not in any way be considered a sale by AT&T to TWE because AT&T literally has nothing to do with (and derives no economic benefit from) any such sale.

Similarly, the sale of programming by Rainbow to TWE should not affect AT&T's insulation in the TWE partnership, because AT&T in no way controls Rainbow. AT&T holds a 33 percent equity investment in Cablevision, which, in turn, owns 75 percent of Rainbow, with the remaining 25 percent held by NBC Cable. AT&T's interest in Cablevision is held only through Class A common shares. The supervoting Class B shares held by the Dolan family and trusts in favor of certain Dolan family members reduce AT&T's voting power to approximately 8.9 percent. AT&T has the right to nominate two of the total 15 members of the Cablevision Board. However, the Class B shareholders are entitled to elect 75 percent of Cablevision's Board. Through their Class B shares, the Dolan family and certain trusts in favor of members of the Dolan family control the Cablevision Board. Thus, Cablevision (and the Dolan family), not AT&T, controls the Rainbow programming services. If Rainbow sells programming to TWE, it does not do so at the direction of AT&T.[94]

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[93] *Jones-Qwest Order* ¶ 29.

[94] In a recent Order, the Commission indicated that "a contractual arrangement to provide programming would be inconsistent with the insulation criterion that 'the limited partner may not perform any services for the partnership materially relating to its media activities,'" and therefore would not allow insulation of the limited partner's interest. Regardless of the merits of that
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c. MediaOne does not manage or control any programming.

MediaOne also controls no programming. For example, MediaOne owns a 5.5 percent interest in The Food Network, which is controlled by Scripps; a 10.4 percent interest in E! Entertainment Television, which is controlled by Comcast and Disney; and a 14.62 percent interest in the Sunshine Network, which is controlled by News Corporation. In addition, MediaOne holds non-controlling interests in four other programming partnerships in which no single entity owns a majority of the partnership interests. MediaOne does not manage any of these programming entities, let alone have the ability to control or compel any actions taken by them. Under such circumstances, it makes no sense to view a sale of programming by these entities as a sale by MediaOne – or AT&T post-Merger.

d. The limited economic interest AT&T is acquiring in video programming raises no competitive concerns.

As noted above, AT&T currently does not control – or have any economic interest in – Liberty programming, and AT&T will not gain the ability to control any significant programming from its acquisition of MediaOne. AT&T will gain *no* ability to dictate what programming these entities develop, or to whom and at what price these entities sell programming.

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decision, however, the sale of programming to TWE by Liberty, Rainbow (a subsidiary of Cablevision), and the video programming providers in which MediaOne holds an interest should not be equated with the sale of such services by AT&T itself. Simply put, the sale of programming to TWE by an entity that is not the "alter ego" of AT&T does not involve AT&T in the media-related business of TWE in any material sense. Report and Order, *Review of the Commission's Regulations Governing Attribution of Broadcast and Cable/MDS Interests*, FCC 99-207, ¶ 133 (rel. Aug. 6, 1999) (citation omitted).

Accordingly, Opponents' Herfindahl-Hirschman Index ("HHI") calculations[95] – which treat these economic interests as full control – make no economic sense. Rather, as set forth in detail in the accompanying CRA Report, unlike control, the limited, silent ownership interests AT&T will acquire through this Merger have, at most, only a very slight – and, here, immaterial – impact on its pricing incentives.[96] While the HHI analyses undertaken by Opponents cannot account for the difference between full control, partial control, and silent financial interest, the modified ("MHHI") analysis set forth in the CRA Report conservatively reflects these factors.[97] And this analysis makes clear that the proposed Merger poses no threat of undue concentration in the video programming marketplace.

This is true whether the relevant market is defined to include basic and premium cable programming services or premium services only. If the relevant market is defined to include basic and premium video programming services, the Merger increases the MHHI by only 48.[98] If the relevant market is defined to include only premium video programming services, there is *no* alteration of the MHHI, because AT&T does not at present own any interests in premium services.[99] Thus, as demonstrated in the CRA Report, the proposed Merger does not result in

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[95] *See* Cooper Report at 54.

[96] CRA Report at 12-15.

[97] *See id.* Appendix A.

[98] *See* CRA Report at 13 & Table 1.

[99] This same result is obtained if the relevant market is defined to include only premium video programming services except Encore because, as noted above, AT&T does not currently own any interests in premium services. Encore could be excluded from premium services because it typically offers second-run movies as compared to the first-run movies and similar programming offered by premium services such as Showtime and HBO.

any material increase in concentration of the video programming business, and the change in concentration resulting from the Merger "is only a small fraction of that estimated by [CU]," and presents little competitive concerns.[100]

2. The Merger Will Not Give AT&T Monopsony Power or Vertical Foreclosure Power.

In the Public Interest Statement, Applicants demonstrated that there is no basis in economics, established antitrust law, or experience to credit claims that this Merger will confer on AT&T monopsony or vertical foreclosure power over unaffiliated video programmers.[101] Post-Merger, AT&T will purchase programming or be involved in programming decisions for cable systems that serve only about a quarter of current MVPD subscribers.[102] There can be no credible claim that AT&T will have power over price or significantly raise rival programmers' costs when they can reach *three fourths* of their potential U.S. customers through other MVPDs, whose programming decisions will be uncontrolled and uninfluenced by AT&T. As the Commission has already recognized, the "over 50 million subscribers" served by other U.S.

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[100] CRA Report at 15. Moreover, even if Liberty were owned and controlled by AT&T for the purpose of a video concentration analysis (which is emphatically not the case), the Merger would increase the MHHI for the cable programming marketplace by at most 104 points, one tenth of the change in the HHI estimated by CU. As noted by CRA, "the competitive effects of these small increases in concentration, even if they were empirically important, could likely be easily offset by the entry of new program services (including additional services from existing providers)." *Id.* at 14. These calculations assume that AT&T's interest in TWE. If one assumes that AT&T has proportional control over TWE following the Merger, then the change in the MHHI is even smaller. *See id.* at 14, n.18.

[101] Public Interest Statement at 54-60. *See also* Declaration of Madison Bond ¶ 20 ("Bond Decl.") (Statement of AT&T's Executive Vice President for Programming that he has "been advised that AT&T ... receives no economic benefit from Liberty Media success, and [he] act[s] accordingly.").

[102] *See* Public Interest Statement at 55-56.

cable companies are alone "well over the threshold for national success"[103] under even the most extravagant estimates that "success" requires 15 to 20 million subscribers.[104] Moreover, the presence and success of DBS providers – with their national coverage and 10 million strong (and rapidly growing) subscriber base – removes any doubt that an attempt by AT&T to mistreat programmers would be not merely futile, but suicidal. Any cable company foolish enough to attempt that would succeed only in driving its intended "victims" into the arms of its DBS competitors, who would be all too happy to embrace spurned but desirable programming – and ultimately the cable company customers that are attracted to that programming.

It should therefore come as no surprise that not a single video programmer filed comments in this proceeding. Moreover, the ILECs and others that purport to champion programmers' interests simply disregard the facts. Their principal claim is that AT&T has the numbers wrong, and that rather than focusing on the relevant criterion – the share of subscribers for which AT&T will purchase programming or be involved in programming decisions – the Commission should instead look to the "homes passed" and "cable-only" criteria that it has already tentatively rejected as a measure of cable MSO power over programmers.[105] Tellingly, the LECs could not muster a single economist to support that approach. To the contrary, the

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[103] Memorandum Op. and Order on Reconsideration and Further Notice of Proposed Rulemaking, *Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Horizontal Ownership Limits*, 13 FCC Rcd. 14462, ¶ 45 (1998) ("*Horizontal Ownership Further NPRM*").

[104] *See, e.g.*, Ameritech at 35. That the 15-20 million figure is unquestionably too high is confirmed by the commercial success of many video programming services with far fewer subscribers. *See, e.g.*, TCI Horizontal Ownership Comments at 76-77.

[105] *Further NPRM* ¶ 76.

only economic affidavit they chose to submit on the subject acknowledges that the focus must be on "subscribers" for which AT&T has "control over buying decisions for cable programming content" and on "alternative buyers" of video programming.[106]

The ILECs nonetheless declare that "new channels would be foreclosed from reaching almost two-thirds of the market if AT&T/MediaOne, for whatever reason, refused their request for carriage."[107] That is patently false. Even under a static analysis, a service that AT&T absolutely refused to carry would still have access to MVPDs that serve three-fourths of all U.S. subscribers. And, as noted above, that static view vastly *overstates* AT&T's position under any dynamic analysis that properly recognizes that a cable company's refusal to carry programming its customers want simply sends those customers to the cable company's DBS and other competitors.[108]

SBC claims that because DBS competition does not constrain cable's "power" over *consumers*, the Commission can ignore the obvious constraint DBS providers place on cable's "power" over *programmers*.[109] Even if the premise were true, the conclusion would not follow.

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[106] *See* Hausman Decl. ¶¶ 11, 14, 22. *See also* CRA Report at 22-23.

[107] GTE at 13.

[108] *See, e.g.*, CRA Report at 24-25; Bond Decl. ¶ 5. SBC "questions the Commission's conclusion in the *1998 Annual Competition Report* that no single cable operator or pair of cable operators is large enough to block entry by a new programmer," SBC at 27, on the basis of Professor Hausman's statements that programmers "will produce lower quality programming" and "may decide to forgo entry altogether" *if* "rates are depressed below competitive levels." Hausman Decl. ¶ 19. But that begs the relevant question whether subscription rates will, *in fact*, be depressed below competitive levels – *i.e.*, whether the cable company in question will have monopsony power. *See, e.g.*, CRA Report at 18-27. As explained above, the facts shown in this proceeding (and those relied upon by the Commission in the *1998 Annual Competition Report*) demonstrate that the answer to *that* question is no.

[109] SBC at 21; Hausman Decl. ¶ 9.

Indeed, even if one were to assume (counterfactually) that cable and DBS were not substitutes *at all* and served entirely distinct customer bases, DBS providers – which clearly *buy* from the same video programmers – would nonetheless remain alternative programming *outlets*, whose existence would fully constrain the ability of a cable MSO to squeeze programmers on price.

In any event, the premise is false.[110] As the Department of Justice has observed:

> Cable and DBS are both MVPD products. While the programming services are delivered via different technologies, consumers view the services as similar and to a large degree substitutable. Indeed, most new DBS subscribers in recent years are former cable subscribers who either stopped buying cable or downgraded their cable service once they purchased a DBS system.[111]

And, as the Commission recently emphasized, "the degree of . . . competition" between the two can only "increase"[112]; *two out of every three* new MVPD subscribers choose a DBS operator over the local cable operator.[113]

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[110] *See, e.g.*, CRA Report at 16-18.

[111] Complaint, *United States v. Primestar, Inc.*, No. 1:98CV01193, ¶ 63 (D.D.C. May 12, 1998).

[112] Order and Authorization, *Application of MCI Telecommunications Corp., Assignor, and Echostar 110 Corp., Assignee*, FCC 99-109, ¶ 19 (May 19, 1999) (emphasis added) (citing DOJ's comments filed in that proceeding) ("*Echostar Order*").

[113] *Fifth Annual Video Competition Report* ¶ 62. Moreover, the DBS subscriber base is growing *over 20 times faster* than the cable subscriber base. *Id.* ¶ 12. As the CRA Report explains (at 17), Professor Hausman is plainly wrong in suggesting that the mere *direction* of recent cable and DBS rate changes undermines the conclusion that consumers view DBS as a substitute for cable. As the Commission has recognized, and as Hausman admits in a footnote, cable rate increases reflect sky-rocketing programming costs (that themselves belie any notion that programmers must be protected from cable companies). And Hausman simply ignores the most obvious explanations for declining DBS prices – *e.g.*, declining equipment costs and an exploding customer base across which to spread fixed costs. Likewise, the "high upfront costs" and "lack of local stations" cited by Hausman as DBS handicaps are already (in the case of former) or will soon be (in the case of the latter) relics of the past, and, in all events, have not stopped two out of three new customers from preferring DBS over cable. Likewise, the fact that cable prices are lower in overbuilt areas does not mean that DBS does not impose constraints on
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SBC next speculates that even if video programmers have far too many alternative outlets to fall prey to AT&T alone, AT&T might collude with other cable companies to drive down programming prices or foreclose disfavored programming.[114] Even ignoring SBC's failure to provide a shred of evidence that this Merger will encourage such patently unlawful conduct, the civil and criminal antitrust laws and authorities have proven quite capable of dealing with price-fixing and other cartel behavior of the kind that SBC hypothesizes. And SBC is certainly wrong in asserting that a risk of "coordination" among MSOs distinguishes this case from the many precedents holding that arrangements that create a buyer of less than 35 percent of the input in question do not even merit review. The Department of Justice has routinely applied that "safe harbor" to cases involving coordinated purchases by unaffiliated providers.[115] Indeed, the safe harbor is so low precisely *because* it is designed to allay both unilateral and coordinated conduct concerns. Consistent with the underlying theory that a successful monopsony or foreclosure strategy must leave suppliers no alternative but to deal with the putative monopsonist, the courts have consistently found that much higher market shares are a prerequisite for the *unilateral* exercise of market power, particularly where, as here, the sellers are sophisticated, large corporations.[116]

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cable prices; it simply means that additional entry has, on occasion, caused prices to fall further. *See* CRA Report at 17.

[114] Hausman Dec. ¶ 12 n.19; *cf.* CRA Report at 22 (explaining why Hausman's "tacit joint bargaining" theory makes no economic sense).

[115] *See* Public Interest Statement at 57 & n.141 (citing letters).

[116] *See* Public Interest Statement at 57-58 & nn.142-143 (citing cases). GTE badly mischaracterizes *Twin City Sportservice, Inc. v. Charles O. Finley & Co.*, 676 F.2d 1291 (9th Cir. 1982). That case had nothing to do with monopsony power, and the district court's holding that a 24 percent share was "*not* sufficient to support an actual monopolization claim," was not even
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SBC, Ameritech and CU attempt to bridge the gap between their allegations and the economic realities by reference to allegations made by the Federal Trade Commission ("FTC") in connection with Time Warner's 1996 transaction to acquire Turner Broadcasting. But the FTC has long stressed that its unproven allegations settled by entry of a consent decree do not have precedential value. *See Beatrice Foods Co.*, 86 FTC 1 (1975) (citing *United States v. DuPont Co.*, 366 U.S. 316, 330 n.12 (1961)) ("[A] consent order entered into by the Commission is not an adjudication on the merits of a matter and is not binding. The Commission in such a proceeding does not determine the legality or illegality of the conduct involved, consent orders contain no complete findings of fact, and many of the factors considered are known only to the Commission and are not a part of the public record").[117]

In all events, whatever the merit of the FTC's concerns in the 1996 deal, they are not remotely plausible here. As described above, AT&T will continue to have no control over (or economic interest in) Liberty's programming; the Time Warner programming (and cable) interests managed by the TWE partnership in which MediaOne has a minority interest will remain completely insulated from AT&T control; and the directly-held MediaOne programming interests that AT&T will acquire are, by any measure, insignificant.[118] Most fundamentally,

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appealed. *Id.* at 1301 (emphasis added). Rather, the appellate court addressed only the district court's holding that certain "exclusive-dealing" arrangements were an "unreasonable restraint of trade" in violation of the Section 1 of the Sherman Act. *Id.* at 1301-05.

[117] *See also Langton v. Hogan*, 71 F.3d 930, 935 (1st Cir. 1995) ("The way in which a consent judgment or consent decree resolves, between the parties, a dispute over a legal issue is not a ruling on the merits of the legal issue").

[118] *See generally* Coffee Decl. & Coffee Supp. Decl. By virtue of this insulation, even if vertical foreclosure were somehow possible despite the many non-AT&T outlets available to unaffiliated programmers, Liberty shareholders, not AT&T, would receive any economic benefit to Liberty programming interests favored by such foreclosure. The significant costs to AT&T of such a
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however, the consent order entered by the FTC already *forbids* Time Warner from engaging in the discrimination against unaffiliated programmers that SBC, Ameritech, and CU posit and would have the Commission attribute to AT&T.[119] Therefore, this Merger cannot have the potential effects that were raised by the FTC.

Finally, GTE points to the Commission's 1993 statement that the need to assure a diversity of information sources might support limits below what traditional antitrust analysis would support.[120] As explained above and in the Public Interest Statement, limits approaching AT&T's post-Merger size *are* well below those that traditional analysis would support. More fundamentally, once concerns about the size and number of MSOs are untethered from the economic rationales of monopsony and vertical foreclosure, there is no obvious – and certainly no demonstrated – link between those concerns and the diversity of information sources available to any MSOs customers.

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strategy – from the customers lost by refusing to carry popular programming – would deter AT&T from attempting foreclosure even if it had the ability. *See* CRA Report at 44-50. *See also* Bruce M. Owen & Steve S. Wildman, *Video Economics* 235-36 (1992) ("It is in the economic interest of MSOs to encourage new program services, because new program services enhance the demand for cable service").

119 Of course, existing Commission rules that apply to *all* cable operators also, *inter alia*: (1) prohibit a cable operator from causing an affiliated programmer to "improperly influence the decision of such vendor to sell, or unduly or improperly influence such vendor's prices, terms and conditions," 47 C.F.R. §§ 76.1001, (2) prohibit a cable operator from discriminating against an unaffiliated programmer in the terms or conditions of carriage based on the programmer's nonaffiliation with the cable operator, 47 U.S.C. § 536(a)(3); 47 C.F.R. § 76.1301(c), and (3) require cable operators to set aside significant capacity on their cable systems to non-affiliated video programmers at reasonable rates. 47 U.S.C. § 532; 47 C.F.R. § 76.970 *et seq*. Moreover, as discussed below, as the Commission has gained more experience with these issues, it has strengthened and expanded these rules.

120 GTE at 12. *See also* CU at 15-17.

Consumers buy programming *locally*. Whether the owner of the MSO in Dallas also owns the MSO in Atlanta has no impact whatever on the diversity of information sources available to viewers in either Dallas or Atlanta. In either case, viewers in each city have access to whatever information the MSO *in their area* provides, in addition to the information supplied via satellite, broadcast, Internet, telephone lines and the myriad other vehicles for delivering information.[121] Nor can there be any claim that large MSOs are less likely to offer diverse programming than their smaller counterparts or that program diversity decreases as concentration increases. Indeed, the available empirical data suggest that the opposite is true.[122] Program diversity, over both cable and the many alternatives to cable, has dramatically increased even as MSO concentration has increased.[123]

In short, the commenters that address the issue provide no coherent theory how AT&T could exercise monopsony power or foreclose rival programming. And, the skyrocketing prices that AT&T and other MSOs pay unaffiliated programmers[124] lend an air of unreality to Opponents' claim that AT&T will have the upper hand. This disconnect largely reflects a failure to acknowledge key factors in the bargaining power equation. Video programmers are often

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[121] *See, e.g.*, Owen & Wildman, *supra* note 118, at 236 ("cable MSOs are not the only gatekeepers" of information).

[122] *See* CRA Report at 42-45 & Appendix D; Stanley M. Besen and John R. Woodbury, "An Economic Analysis of the FCC's Cable Ownership Restrictions," at A-1 (Aug 14, 1998) (attached to Comments of TCI, *In the Matter of Implementation of Section 11(c) of Cable Television Consumer Protection and Competition Act of 1992 – Horizontal Ownership Limits*, MM Docket No. 92-264 (Aug. 14, 1998)).

[123] As described in the Public Interest Statement and in the Commission's Annual Competition Reports, there has been a dramatic increase in the deployment of new technologies capable of bringing both video programming and other information directly to the consumer. *See, e.g.*, Public Interest Statement at 46-54; *Fifth Annual Video Competition Report* ¶ 102 & n.451.

[124] *See, e.g.*, Bond Decl. ¶ 9; *Fifth Annual Video Competition Report* ¶¶ 9, 24.

themselves very large and sophisticated commercial actors that hold *exclusive* rights to unique programming content that subscribers demand and without which an MSO would be competitively handicapped.[125] This "clearly mitigates" any "buying power."[126] MSO "buyer power" is further constrained by the existence of alternative outlets for video programming, including not only direct cable competitors like DBS, but also numerous broadcast, international cable, and videotape outlets.[127] Any remaining concern about MSO monopsony or vertical foreclosure is dispelled by the digital and other cable upgrades that increase channel capacity and thus MSO *demand* for more and more distinct programming.[128] These factors, together with the undeniable force of DBS competition, explain both why the video programmers have stayed on the sidelines in this proceeding and why the claims of others that AT&T will squeeze programmers are entirely without merit.

3. The Merger Will Not Violate the Cable Act or the Commission's Rules.

Unable to show that the Merger has any anticompetitive impact on video programming, the ILECs and other AT&T competitors raise various Cable Act-related objections and propose a number of conditions to the proposed Merger. As shown below, these objections and proposed conditions are without merit and should be rejected.

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[125] *See* Bond Decl. ¶¶ 4-5. It is well established that highly differentiated products such as video programming are not perfect substitutes and that firms that manufacture highly differentiated products are more capable of unilaterally exercising market power. *Horizontal Merger Guidelines* § 2.21.

[126] Michael E. Porter, *Competitive Strategy: Techniques for Analyzing industries and Competitors* (1980). *See also* Bond Decl. ¶¶ 3-9.

[127] *See* CRA Report at 40.

[128] *See United States v. Syufy Enterprises*, 903 F.2d 659, 670-71 (9th Cir. 1990) (recognizing that purchasers who have excess capacity are in an extremely weak bargaining position).

a. **Horizontal rules.**

i. **The Merger will not violate any Commission rule or statute concerning horizontal concentration.**

Several Opponents urge the Commission to deny the Merger because the post-Merger AT&T will exceed the cable horizontal ownership limit.[129] However, after the D.C. District Court found the statutory horizontal ownership provision unconstitutional, the Commission voluntarily stayed its 30 percent homes-passed limit[130] and affirmed this stay just last year.[131] Thus, there is no horizontal ownership limit currently in effect that the post-Merger AT&T will exceed. For this reason alone, the Commission should deny these claims.

Denial of these claims is also warranted by AT&T's commitment to the Commission that if and when the court pronounces the statutory provision constitutional, "AT&T will comply with whatever ownership limits emerge from the current judicial and Commission proceedings."[132] In fact, the Commission has already made clear that such a result would be required,[133] and so no further action by the Commission is necessary to ensure compliance with any future horizontal ownership limit that passes constitutional muster.[134]

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[129] Ameritech at 7-9; Bell Atlantic at 7-9; CU at 4-13; GTE at 7-14; SBC at 11-14; U S West at 4-13.

[130] *See* Second Report and Order, *In the Matter of Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992 - Horizontal and Vertical Ownership Limits,* 8 FCC Rcd. 8565, ¶ 3 (1993) ("*Horizontal Ownership Order*").

[131] *See Horizontal Ownership Further NPRM* ¶ 75.

[132] Public Interest Statement at 67.

[133] *See Horizontal Ownership Further NPRM* ¶ 77.

[134] SBC and CU claim that AT&T failed to provide in its Applications a certification regarding homes passed required by 47 U.S.C. § 76.503(c). However, as AT&T recently explained in its opposition to CU's motion to dismiss the Application, this is simply not true. Rule 76.503(c)

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ii. Current marketplace conditions justify adoption of AT&T's proposed amendments to the cable horizontal ownership rule and the underlying attribution rule.

Opponents' claims that the Commission should deny the Application because AT&T post-Merger will exceed 60 percent of cable homes passed are pure sophistry. The Commission has already tentatively concluded that its cable homes-passed rule should be changed in the pending *Horizontal Ownership Further NPRM.*[135] More fundamentally, the Opponents completely ignore marketplace and regulatory developments since 1993 that effectively "check" any MSO's ability to engage in the type of conduct that the cable horizontal ownership limit is designed to prohibit – *i.e.*, extracting unfair concessions from programmers (monopsony power), foreclosing entry by rival programmers (vertical foreclosure), or otherwise reducing program diversity. The most important of these checks are the following:

- *The increase in MVPD competition.* When the Commission adopted the suspended horizontal rule in 1993, DBS had not even been launched. Today, DBS has over 10 million subscribers. It is a fact that programmers today have *many* more alternatives than they did in 1993, and this reduces the ability of any MSO to harm the programming market.[136]

- *Other regulations that target the very same concerns addressed by the horizontal ownership limit.* A number of other cable regulations, including the must carry, program carriage, channel occupancy, PEG access, and leased access rules,

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requires no such certification in an application for transfer of control – or, indeed, *any* certification in an application. Rather, the rule requires only that the necessary certification be made "[p]rior to acquiring additional cable systems." *See* Opposition of AT&T Corp. and MediaOne Group, Inc. to Motion to Dismiss, CS Docket No. 99-251, at 1 (filed Aug. 23, 1999). Moreover, even though AT&T was not required to provide any certification under Section 76.503(c) in its Applications, the Applications did in fact include the relevant cable homes passed information – both before and after the Merger.

[135] *See Horizontal Ownership Further NPRM* ¶¶ 80-81, 84-86.

[136] *See* Public Interest Statement at 46-54; and Section II.A, *supra*. *See also* Comments of AT&T on Video Competition NOI, CS Docket No. 99-230, at 1-21, filed August 4, 1999.

already prohibit MSOs from acting in ways that harm programmers or reduce diversity. Moreover, the experience the Commission has gained with these rules reveals that they have been an effective method of checking any possible monopsony and vertical foreclosure power that MSOs may possess, and of ensuring programming diversity.[137] For example, in the six years since their adoption, not a single complaint has been filed under the channel occupancy rule and the only program carriage complaint was settled by the parties. This strongly supports AT&T's view that the concerns underlying the cable horizontal ownership limit are less significant today than they were thought to be in 1993.[138]

- *Digital deployment.* Digital technology is already expanding channel capacity. By providing programmers with additional capacity for distribution of their program services, digital technology further reduces concerns about harm to the programming market. In fact, the Commission already has acknowledged that expanded channel capacity has the effect of discouraging cable operators from exercising monopsony power, engaging in vertical foreclosure, or otherwise reducing diversity. This is the very reason the Commission decided not to apply the channel occupancy limit for channels in excess of 75 on a given cable system.[139]

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[137] Moreover, some of these rules have been strengthened and expanded since the Commission originally considered them in the context of the horizontal ownership limit. For example, the Commission has significantly enlarged the rights of complainants under the leased access and program access rules, and the Supreme Court has affirmed the constitutionality of the must carry rules. *See* Comments of TCI, MM Docket No. 92-264, at 21-26 (filed August 14, 1998), for a more detailed discussion of the experience with, and strengthening of, these rules since 1993.

[138] Thus, GTE's (at 12) and U S West's (at 11) arguments that the Commission already considered these rules when it adopted the 30 percent homes-passed limit are inapposite. Because the Commission had little experience with these regulations at the time the suspended horizontal rule was adopted, it was not able to give them adequate weight. Similarly Opponents' suggestion that these other rules are not as effective as "structural" regulations is plainly wrong. For example, the channel occupancy rule is a structural, "easy-to-detect" and "easy-to-enforce" regulation (to use the Commission's terminology). The must carry rule is also not a behavioral regulation and, like other structural regulations, is easy to detect and enforce.

[139] *Horizontal Ownership Order* ¶ 83 ("We continue to believe that expanded channel capacity will reduce the need for channel occupancy limits. . . . [T]he expanded channel capacity that will result from fiber optic cable and digital compression technology will help obviate the need for such limits as a means of encouraging cable operators to carry unaffiliated or competing video programming services. . . . [T]he record indicates that vastly larger cable systems will likely be inclined to deliver targeted 'niche' video programming services aimed at correspondingly smaller audience sizes").

The Commission itself has provided dramatic evidence that concerns about the programming market are far less significant today than they were in 1993. It has pointed out year after year in its annual competition reports that independent programming sources have exploded over the last six years,[140] despite the fact that the horizontal ownership limit has never been enforced during this period and that AT&T has already acknowledged in its periodic Section 76.504(c) notification letters to Commission that it is over the suspended homes-passed limit. And even as they increase in number, video programmers have been rapidly escalating the license fees they demand (and get) from MVPDs – irrefutable evidence that in today's competitive environment the programming sellers are in a strong bargaining position and are in little need of protection from the overly restrictive Commission rules.[141]

The foregoing developments *alone* justify changes to the horizontal ownership limit and associated attribution rules. Moreover, AT&T has proposed to modify the attribution rules in ways that would further protect against any conceivable harm to the programming market. Under AT&T's proposal, an MSO would not bee deemed to have an attributable interest where the following two conditions were met:

1) *The MSO may not buy programming for the system.* This requirement directly addresses the concern that an MSO could use an interest in a cable system to obtain unfair concessions from programmers (monopsony power). An MSO would derive no additional buying power from a cable system for which it does not purchase programming, even if the MSO has a minority interest in the system.

2) *The MSO may not be involved in, or have access to any information regarding, the programming decisions of the system.* This requirement directly addresses concerns about vertical foreclosure and reducing program diversity. If an MSO agrees not to be involved in a cable system's programming choices and not to have access to any information regarding such programming (including

[140] *See* Section II.A.1, *supra.*

[141] *See* Bond Decl. ¶ 9.

> programming contracts), then it cannot pursue a strategy of foreclosing a rival program service on that system or of slanting the programming toward the MSO's viewpoint.

AT&T recognizes that several parties objected to the discussion of the "no program purchase or control" rule in the Public Interest Statement, claiming that a focus on "control" over programming decisions ignores the Commission's concerns about influence.[142] Although AT&T continues to believe that a focus on control serves the underlying purposes of the cable horizontal ownership rule, the "no program purchase or involvement" focus unquestionably answers these questions.[143]

Adoption of AT&T's proposed test is further supported by the significant benefits to local telephone and broadband competition that the Merger will create, as discussed, *supra*, and in the Public Interest Statement. When Congress adopted the horizontal ownership provision in the 1992 Cable Act, it specifically instructed the Commission to take account of the fact that cable networks were evolving rapidly and had the potential to provide consumers with a vast array of new technologies and services.[144] When Congress spoke again in the 1996 Act, it emphasized the need to develop local telephony and broadband competition, and noted the unique role that cable companies could play in developing such competition. And when the

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[142] CU at 12-13; GTE at 13-14.

[143] To implement this rule in the most efficient manner possible, the MSO could be required to certify to the Commission that it complies with these two conditions in order to avoid attribution under the horizontal rules. As AT&T has previously noted, such a certification process is well-established under Commission precedent regarding attribution. *See* TCI Comments, CS Docket No. 98-82, at 19-25 (filed Aug. 14, 1999).

[144] For example, Congress mandated that the Commission "account for any efficiencies and other benefits that might be gained through increased ownership or control" of cable systems, 47 U.S.C. § 533(f)(2)(D), and that it adopt rules that "reflect the dynamic nature of the communications marketplace," *id.* § 533(f)(2)(E).

Commission approved the AT&T-TCI merger, it noted that it is "committed to ensuring that residential local exchange competition becomes a reality *sooner rather than later*."[145] It would be absurd and unfortunate if AT&T's customers were denied the 1996 Act's promised benefits – competitive local telephony and new broadband services – because of a needlessly restrictive limit on cable horizontal ownership.

iii. AT&T did not ignore the Commission's existing attribution Rules.

Contrary to the claims of a few parties,[146] the Applications did not ignore the Commission's *suspended* attribution rules when discussing AT&T's size post-Merger. Appendices A and B of the Public Interest Statement contain, among other things, a list of all cable systems in which AT&T and MediaOne hold interests (including systems in which AT&T or MediaOne hold only partial interests and do not purchase or control programming), so that any party can determine which systems would be potentially attributable to AT&T even under the current attribution rules.

Proposals that the Commission apply the broadcast attribution rules are misguided. The broadcast rules were developed specifically to prevent anticompetitive practices between *competing* broadcasters. The fundamental concern underlying these rules is that competing broadcasters will exert horizontal market power that will diminish competition and program diversity in the *local* market. As Drs. Besen, O'Brien, Woodbury, and Moresi describe:

> The Commission is concerned about local broadcast market competition because if one broadcast station acquires a silent financial interest in a rival broadcast station in the same

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[145] *AT&T-TCI* ¶ 48 (emphasis added).

[146] *See* CU at 12-13, 22-24; GTE at 13-14; U S West at 7-10.

geographic area, the investing station may have a reduced incentive to compete for advertisers and viewers. This is because some of the advertisers and viewers who would switch to the investing station if it lowered advertising rates or improved programming will be drawn from the acquired station. Because the investing station shares in the profits of the acquired station by virtue of its financial interest, its incentives to compete with that station are thereby reduced.[147]

By contrast, cable systems do not generally compete with each other in the same geographic areas for subscribers, local advertising revenues, or for programming. Consequently, there is no possibility that acquiring an interest in another cable system will reduce the level of competition among the systems for subscribers or for local advertisers and thus there is no risk that the investment of one cable system in another will result in higher prices to subscribers and advertisers.[148] As the CRA Attribution Analysis concludes, "[t]his suggests that the attribution rules for the cable industry should be more lenient than those for the broadcast industry."[149]

This conclusion is especially true with respect to the cable horizontal ownership limit. As noted, the fundamental concern underlying this limit has nothing to do with preventing market power at the *local* level, but rather with preventing market power at the *national* level.[150] As AT&T has explained in comprehensive economic analyses submitted to the Commission,

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[147] *See* Stanley M. Besen, Daniel P. O'Brien, John R. Woodbury, and Serge X. Moresi, Charles River Associates, "An Economic Analysis of the Effects of Partial Ownership Interests in Cable Systems," August 14, 1998, at 17 (filed as an attachment to the Comments of TCI filed in CS Docket No. 98-82 on August 14, 1998) ("CRA Attribution Analysis").

[148] *See FCC Policy On Cable Ownership: A Staff Report by Kenneth Gordon, Jonathan D. Levy and Robert S. Preece* ¶ 93 (Nov. 1981) ("Only in markets where MSOs compete directly with one another could problems of horizontal market power arise. Thus it is clear at the outset that such [market power] problems cannot arise in the local distribution function of cable, since different systems do not compete directly against one another.") (citations omitted).

[149] CRA Attribution Analysis at 18.

[150] *See Fifth Annual Video Competition Report* ¶¶ 125, 152-153.

these national programming concerns pose smaller competitive and diversity risks than the local market power concerns underlying the broadcast attribution rules.[151]

iv. Failure to allow horizontal ownership of 35 percent for cable, after just raising the limit for broadcasters to 35 percent, would be arbitrary and capricious.

While, as shown above, fundamental competitive differences between the broadcast and cable industries make application of the broadcast attribution rules to the cable industry inappropriate, there is no basis in logic or economics that would permit the Commission to set a lower horizontal ownership limit for cable systems than the 35 percent level it adopted for broadcasters.

In raising the broadcast horizontal ownership limit, the Commission reaffirmed its view of broadcasters as a "uniquely important" distribution mechanism in terms of ensuring programming diversity. "There is consequently a vital public interest in ensuring that these influential outlets for communications are in the hands of a broad number of different owners."[152] But if a 35 percent horizontal ownership limit is not too high to cause concerns about monopsony, vertical foreclosure, or diversity for the "uniquely important" broadcasters, *a fortiori*, it cannot reasonably be viewed as a problem for the cable industry, particularly given the

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[151] *See generally* CRA Attribution Analysis.

[152] *See Review of the Commission's Regulations Governing Television Broadcasting,* Television *Satellite Stations Review of Policy and Rules,* MM Docket Nos. 91-221 and 87-8, ¶ 18 (rel. Aug. 6, 1999). The Commissioners echoed these conclusions in their individual statements. Commissioner Ness, for example, observed that "broadcasting remains a distinctly special service – with unique privileges and unique responsibilities." Statement of Commissioner Ness at 2. Commissioner Powell agreed that the "free business model [of broadcasters] is quite unique and . . . warrants some government attention to undue concentration." Statement of Commissioner Powell at 2.

industry's well-established track record in promoting diverse programming notwithstanding increases in MSO size.[153] This is especially true when one considers that under the broadcast limit the Commission only counts 50 percent of homes reached by UHF (and also grandfathers LMAs and exempts satellite TV stations), so that broadcasters are able to own stations that reach substantially more than 35 percent of all television households.[154]

b. Program access rules.

i. The Commission should not subject AT&T's terrestrially distributed programming services to the program access rules.

Certain Opponents claim that the Merger will give AT&T the ability and incentive to circumvent the program access rules by delivering programming terrestrially (as opposed to using satellite delivery). They therefore urge the Commission to condition approval of the Merger on AT&T's commitment to make all its affiliated programming services subject to the program access restrictions, *regardless* of whether they are satellite or terrestrially delivered.[155]

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[153] CU's suggestion that Congress' silence on the cable horizontal ownership limit in the 1996 Act indicates an intent to leave the limit at 30 percent, is exactly backwards. CU at 20-21. It would have made no sense for Congress to include a provision in the 1996 Act addressing the cable horizontal ownership limit because: (1) the statutory provision had been held unconstitutional; and (2) the rule had been stayed. Since no limit was in effect, there was nothing for Congress to increase. Moreover, because the Commission has broad discretion under Section 613(f)(1) to establish a cable horizontal ownership limit, a separate congressional delegation was not required to authorize the Commission to increase this limit.

[154] *See* 47 C.F.R. § 73.355(e)(2). Further, as the Commission has recognized, must carry requirements and other specific restrictions applicable to the cable industry (but not to broadcasters) also ensure the carriage of diverse programming. *See Horizontal Ownership Order* ¶ 54 ("[C]arriage of broadcast, PEG and leased access channels promotes diversity and provides alternative sources of unaffiliated programming to cable subscribers in furtherance of the statutory objectives.").

[155] *See* Ameritech at 12-17; WCAI at 13-19; Bell Atlantic at 17-20.

However, on three occasions within the last year, the Commission has expressly addressed – and rejected – requests to extend the program access rules to terrestrially delivered programming.

In October 1998, the Cable Services Bureau held that the program access provisions apply only to "satellite cable programming," and not to programming that was "previously" satellite-delivered or the "equivalent" of satellite cable programming.[156] In so ruling, the Bureau reached conclusions that dispose of the various contentions raised here:

> In enacting Section 628, Congress determined that while cable operators generally must make available to competing MVPDs vertically integrated programming that is satellite-delivered, they do not have a similar obligation with respect to programming that is terrestrially delivered. DIRECTV's argument would have us find that it is somehow unfair for a cable operator to move a programming service from satellite delivery to terrestrial delivery if it means that a competing MVPD may no longer be afforded access to the service. We find no evidence in Section 628 that Congress intended such a result.[157]

In its August, 1998 order expanding the program access rules in certain respects, the Commission itself concluded that there is no factual basis for extending the rules to terrestrially delivered services, even assuming that the Commission had authority to do so:

> The record developed in this proceeding fails to establish that the conduct complained of, *i.e.*, moving the transmission of programming from satellite to terrestrial delivery to avoid the program access rules, is significant and causing demonstrative competitive harm at this time. . . . In circumstances where anticompetitive harm has not been demonstrated, we perceive no reason to impose detailed rules on the movement of programming from satellite delivery to terrestrial delivery that would unnecessarily inject the Commission into the day-to-day business decisions of vertically-integrated programmers.[158]

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[156] *See In the Matter of DIRECTV, Inc. v. Comcast Corporation, et al.*, DA 98-2151, ¶ 25 (Oct. 27, 1998).

[157] *Id.* ¶ 32.

[158] *In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992, Petition for Rulemaking of Ameritech New Media, Inc. Regarding*

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And just a few months ago in its Order approving the AT&T-TCI merger, the Commission affirmed this holdings and specifically rejected the very same arguments and proposals raised in this proceeding to extend the program access rules to AT&T's terrestrially distributed programming.[159]

ii. The Commission should not ban exclusive agreements between AT&T and unaffiliated programmers.

Having failed in recent months to convince the Commission to impose any additional limits on programming exclusivity throughout the industry, Ameritech and others attempt to resuscitate their efforts here, claiming, as they did in the AT&T-TCI merger review proceeding, that approval of the proposed Merger should be conditioned on AT&T's commitment not to enter into exclusive agreements with non-vertically integrated programmers.[160] The Commission should reject this proposed condition for the same reasons it rejected it in the AT&T-TCI merger proceeding.[161]

Opponents provide no new legal or policy basis for their proposed outright ban on all AT&T exclusivity arrangements, an outcome that is directly at odds with the approach taken by

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(. . . continued)
Development of Competition and Diversity in Video Programming Distribution and Carriage, 12 Comm. Reg. (P&F) 1296, ¶ 71 (1998) (citations omitted).

[159] *AT&T-TCI* ¶ 37.

[160] *See* Ameritech at 17-18; BellSouth at 2, 5-7; EchoStar at 6, 8-9; SBC at 23-24; WCAI at 3-5.

[161] *AT&T-TCI* ¶ 38 ("We further decline to condition the merger on the imposition of anti-exclusivity restrictions that are not required by the program access rules. If parties believe any existing exclusivity agreements violate the program access rules, the program access complaint process is the appropriate forum in which to resolve such grievances. Commenters have not alleged that existing exclusivity arrangements are unlawful, and we do not find that this merger provides a basis for the Commission to declare unlawful TCI's future exclusivity agreements to the extent they conform with current rules.") (citations omitted).

Congress in the Cable Act.[162] They also fail to recognize that exclusive arrangements can promote efficiencies including, among other things, reduced transaction costs (*e.g.*, dealing with only one distributor for a market) and the elimination of promotional free-riding (which, in turn, creates incentives to promote programming more zealously because the promotional benefits run to the distributor and not its competitors) – efficiencies that the Commission itself has recognized.[163]

Indeed, some of the very same parties who in this proceeding ask the Commission to bar AT&T outright from entering into exclusive arrangements are themselves increasingly using exclusivity as a competitive weapon *against* AT&T and other cable operators. For example, DirecTV has touted its exclusive sports packages (such as "NFL Sunday Ticket,"[164] "NBA League Pass," and "NHL Center Ice") as "not available on cable"[165] and has trumpeted its exclusive music concerts as part of its "tradition of delivering quality programming not available on cable."[166] The

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[162] *See, e.g.*, 47 U.S.C. § 548(c)(2)(C), (D) (permitting exclusivity under all circumstances when there is no vertical integration or no satellite delivery; and permitting exclusivity for vertically integrated programmers in served areas if found to be in the public interest).

[163] *See Amendment of Parts 73 and 76 of the Commission's Rules Relating to Program Exclusivity in the Cable and Broadcast Industries*, 3 FCC Rcd. 5299, ¶ 66 (1988); *see also Program Access Order*, 8 FCC Rcd. 3359, ¶ 65 (1993); *New England Cable News, CSR-4190-P, Memorandum Opinion and Order*, 9 FCC Rcd. 3231, ¶ 37 (1994).

[164] *See Hughes 1998 Annual Report* at 22 (1999) ("DirecTV's important arrangement making it the exclusive small-dish provider of NFL Sunday Ticket has been extended through 2002.").

[165] *See* DirecTV News Release, "DirecTV to Offer Last Six Weeks of '97 NFL Sunday Ticket Free to New Subscribers," (Nov. 3, 1997) <www.directv.com:80/press>; DirecTV News Release, "DirecTV Offers Free Preview of NBA League Pass and NHL Center Ice to Subscribers," (Oct. 3, 1997) <www.directv.com:80/press>.

[166] *See* DirecTV News Release, "Shania Twain's First-Ever Televised Concert to be Broadcast Live Only on DirecTV," (Aug. 17, 1998) <www.directv.com:80/press>; *see* DirecTV News Release, "DirecTV to Air Exclusive Premiere of Tom Petty and Heartbreakers Concert," (July 12, 1999) <www.directv.com:80/press>.

ability of DBS operators to enter into such exclusive arrangements free of the onerous regulations that apply to their cable counterparts is a significant competitive advantage.

iii. The Commission should not mandate the sale of AT&T-affiliated programming at specified volume discounts that exceed the program access rule requirements.

Ameritech requests that approval of the Merger be conditioned upon AT&T's commitment to offer any MVPD the same volume discounts AT&T offers its own affiliated entities.[167] However, just as the Commission rejected CU's proposal to mandate the sale of AT&T-affiliated programming at "market" prices in the AT&T-TCI merger review proceeding,[168] it should reject Ameritech's request here that AT&T provide its programming at specified volume discounts to any and all MVPDs. As the Commission correctly concluded:

> We reject Consumers Union's proposal that the Commission mandate the sale of programming at "market" prices. Neither the merger nor the Commission's rules provide any basis for the imposition of a mandate that Liberty Media price its programming at any particular level, provided the pricing is not unlawfully discriminatory.[169]

There is nothing unique about this Merger that would justify a different conclusion. Moreover, as the CRA Report concludes, more restrictive volume discount rules imposed on AT&T are particularly unjustified given that the economic rationale and data relied on by Ameritech's economic experts are fundamentally flawed.[170]

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[167] *See* Ameritech at 22-23.

[168] *See AT&T-TCI* ¶ 39.

[169] *Id.*

[170] *See* CRA Report at 33-34 ("[Dertouzos and Wildman's ('DW')] estimates of the discount obtained by large cable MSOs are likely to be highly inaccurate and their attempt to ascribe virtually their entire estimated difference to bargaining power on the part of large MSOs is defective because they fail to recognize a large number of cost and efficiency-based explanations that actually exist. . . . [T]he fees paid by cable operators and other MVPDs depend on a wide range of provisions in their contracts with program services. . . . Without taking these, and other,

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c. Channel occupancy rules.

Bell Atlantic contends that AT&T post-Merger will violate the channel occupancy rules because of AT&T's acquisition of interests in MediaOne and TWE programming.[171] Bell Atlantic does not identify any AT&T cable system that it believes would not be in compliance with the channel occupancy rules post-Merger.[172] For this reason alone, the Commission should reject this argument.

Moreover, this Merger proceeding is an inappropriate forum in which to make such generalized allegations. First, the Commission already has an enforcement process in place for handling alleged violations of the channel occupancy rules, and that process should govern here.[173] In fact, this is exactly what the Commission concluded in the AT&T-TCI merger proceeding with regard to program access complaints.[174]

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differences into account, it simply is not possible to compare the prices paid by different operators, but DW's analysis neither recognizes nor controls for these differences.").

171 Bell Atlantic at 9-14.

172 Bell Atlantic states that AT&T is "close to exceeding" the limits in several of its largest markets, and attempts to support that claim by citing the home page of the TV Guide Web site. *Id.* at 11, n.32. That home page, however, makes no reference to AT&T's programming interests in any of its cable systems. *See* <http: //www.tvguide.com> (accessed Aug. 27, 1999).

173 *See* Second Report and Order, *Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992: Horizontal and Vertical Ownership Limits*, Second Rept. and Order, 8 FCC Rcd. 8565, ¶ 99 (1993) ("*Channel Occupancy Order*") (indicating that parties wishing to allege a channel occupancy claim with *respect to a specific system* should notify the relevant LFA or file a particularized complaint with the Commission).

174 *AT&T-TCI* ¶ 38 ("If parties believe any existing exclusivity agreements violate the program access rules, the program access complaint process is the appropriate forum in which to resolve any such grievance.").

Second, because an analysis of a cable system's compliance with the channel occupancy rules would be highly fact-intensive, a merger proceeding is a particularly inappropriate forum for raising such unsubstantiated generalized allegations. For example, to minimize consumer confusion and disruption to existing programming relationships, the Commission grandfathered all vertically integrated video programming services carried on systems as of December 4, 1992 that exceeded the Commission's channel occupancy limits.[175] This grandfathering – which runs to the system and continues indefinitely – alone makes any generalized assertions about channel occupancy violations untenable. In short, given the way the rules operate, one cannot (as Bell Atlantic suggests) simply look at a cable system's channel lineup, match up the services in which the relevant cable operator has an attributable interest, and divide the number of such matched services by the system's total number of activated channels to determine whether the system has exceeded its channel occupancy limit. If Bell Atlantic or any other party believes that an AT&T system has exceeded the limit, it is free to identify the system with a specific complaint and specific factual allegations. As no party has initiated such a complaint, the Commission should not entertain Bell Atlantic's baseless speculations in this proceeding.[176]

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[175] *Channel Occupancy Order* ¶ 93; 47 C.F.R. § 76.504(d) ("Cable operators carrying video programming services owned by the cable operator or in which the cable operator holds an attributable interest in excess of limits set forth . . . as of December 4, 1992, shall not be precluded by the restrictions in this section.").

[176] AT&T notes that in the six years since adoption of the rules, not a single channel occupancy complaint has been filed (let alone an adverse decision rendered) against any AT&T cable system. *Cf.* Errata, *Applications of Craig O. McCaw, Transferor, and AT&T, Transferee, for Consent to the Transfer of Control of McCaw Cellular Communications, Inc. and its Subsidiaries*, FCC 94-238, ¶ 152 (rel. Sept. 19, 1994) ("We find that the public interest would not be served by our withholding action on the proposed merger to conduct further fact finding based on the generalized allegations made by the Ad Hoc IXCs in this proceeding."); Memorandum Op. and Order, *AT&T Corp., et al., Joint Application for Authorization pursuant to Section 214 of the Communications Act of 1934, as amended*, DA 99-1637, 1999 WL 635709,

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Unable to show even a colorable violation of the Commission's Rules, Bell Atlantic resorts to sophistry. It also argues that AT&T must count @Home and Road Runner as two channels each (*i.e.*, one for downstream traffic, a second for upstream signals) for the channel occupancy rules. As the statutory language and Commission regulations make clear, the channel occupancy rules are designed to limit the number of channels on a cable system that can be occupied by a vertically-integrated *video programmer*.[177] Because the Commission has consistently held that Internet-delivered video is not "video programming" under the Communications Act,[178] *a fortiori*, ISP services such as @Home and Road Runner are not video programmers and therefore do not count toward a cable system's channel occupancy limit.[179] In addition, although Bell Atlantic's petition disputes the Commission's determination that ISPs do

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¶¶ 12-14 (Aug. 20, 1999) (denying allegations regarding volume discount abuses and directing the opponents of the license grant to "file a complaint with the Commission pursuant to section 208 . . . [which] should state the particular facts upon which the allegations are based.").

[177] *See* 47 U.S.C. § 533(f)(1)(B); 47 C.F.R. § 76.504(a).

[178] *See, e.g., Fifth Annual Video Competition Report*, ¶¶ 102-105 (noting that "long form video programming offered by Internet video still remains less than broadcast quality"); Order on Reconsideration, *In Re Implementation of Section 207 of the Telecommunications Act of 1996: Restrictions on OTARD*, 13 FCC Rcd. 18962, ¶ 56 (1998) (stating that "video-related services," such as video over the Internet, have not been shown to be comparable to those provided by a television broadcast station).

[179] Bell Atlantic's contention that AT&T's exclusivity arrangements with @Home and Road Runner "strike at the heart" of the channel occupancy rules, Bell Atlantic at 11-13, are similarly unavailing. Because @Home and Road Runner are not video programmers under Commission precedent, these exclusivity arrangements do not even implicate, much less violate, the channel occupancy rules.

not provide video programming, this claim is not merger-specific. As such, it cannot be considered in this proceeding.[180]

d. Program carriage rules.

Bell Atlantic states that AT&T and MediaOne are already violating the program carriage rules by refusing to deal with ISPs other than their own affiliated @Home and Road Runner services.[181] Once again, Bell Atlantic's claim is groundless. The Communications Act and the Commission's rules clearly state that the program carriage restrictions govern agreements between MVPDs and *video programming vendors*.[182] Because, as discussed above, the Commission has consistently held that Internet services do not provide video programming, @Home and Road Runner are not "video programming vendors" that can form the basis of a program carriage discrimination complaint.[183] In addition, like its channel occupancy rule argument, Bell Atlantic's disputes with the Commission's determination have nothing to do with this Merger, and should be considered, if at all, as part of a formal rulemaking proceeding.[184]

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[180] In fact, the Commission is currently considering whether an ISP is a provider of video programming for purposes of the leased access rules. *See* Memorandum Op. and Order, *In re Petition of Internet Ventures, Inc. for Declaratory Ruling Regarding Whether Internet Service Providers are Entitled to Leased Access to Cable Facilities Under Section 612 of the Communications Acts of 1934, as amended*, CSR-5407-L (1999). Bell Atlantic remains free to press its claims there.

[181] Bell Atlantic at 15-16.

[182] 47 U.S.C. § 536(a)(3); 47 C.F.R. § 76.1301(c).

[183] This same conclusion applies to Bell Atlantic's claim that AT&T's limitation on Internet video streaming violates the program carriage rules. Bell Atlantic at 16-17.

[184] Finally, even assuming *arguendo* that @Home and Road Runner did constitute video programming vendors, the proper forum for alleging improper discrimination is a complaint under the program carriage complaint procedures set out in 47 C.F.R. § 76.1302, not this license transfer proceeding.